

**REPORT OF THE AUDIT OF THE
CLAY COUNTY
FORMER SHERIFF'S SETTLEMENT - 2005 TAXES**

June 30, 2006



**CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS
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EXECUTIVE SUMMARY
AUDIT EXAMINATION OF THE
CLAY COUNTY
FORMER SHERIFF'S SETTLEMENT - 2005 TAXES

June 30, 2006

The Auditor of Public Accounts has completed the audit of the Sheriff's Settlement - 2005 Taxes for the former Clay County Sheriff as of June 30, 2006. We have issued an unqualified opinion on the financial statement taken as a whole. Based upon the audit work performed, the financial statement is presented fairly in all material respects.

Financial Condition:

The former Sheriff collected taxes of \$3,012,363 for the districts for 2005 taxes, retaining commissions of \$124,258 to operate the Sheriff's office. The former Sheriff distributed taxes of \$2,886,537 to the districts. Taxes of \$8 are due to the districts from the former Sheriff.

Report Comment:

- The Former Sheriff's Office Lacked Adequate Segregation Of Duties
- The Former Sheriff Should Have Accounted For Delinquent Franchise Taxes Correctly

Deposits:

The former Sheriff's deposits as of November 14, 2005 were exposed to custodial credit risk as follows:

- Uncollateralized and Uninsured \$151,360

The former Sheriff's deposits were covered by FDIC insurance and a properly executed collateral security agreement, but the bank did not adequately collateralize the former Sheriff's deposits in accordance with the security agreement.

CONTENTS

PAGE

INDEPENDENT AUDITOR'S REPORT	1
SHERIFF'S SETTLEMENT - 2005 TAXES	3
NOTES TO FINANCIAL STATEMENT	5
COMMENTS AND RECOMMENDATIONS	8
REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF THE FINANCIAL STATEMENT PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS	15



CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

To the People of Kentucky

Honorable Steven L. Beshear, Governor

Jonathan Miller, Secretary

Finance and Administration Cabinet

Honorable Carl E. Sizemore, Clay County Judge/Executive

Honorable Edward Jordan, Former Clay County Sheriff

Honorable Kevin Johnson, Clay County Sheriff

Members of the Clay County Fiscal Court

Independent Auditor's Report

We have audited the Clay County Sheriff's Settlement - 2005 Taxes as of June 30, 2006. This tax settlement is the responsibility of the former Clay County Sheriff. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States, and the Audit Guide for Sheriff's Tax Settlements issued by the Auditor of Public Accounts, Commonwealth of Kentucky. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1, the Sheriff's office prepares the financial statement on a prescribed basis of accounting that demonstrates compliance with the modified cash basis, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the accompanying financial statement referred to above presents fairly, in all material respects, the former Clay County Sheriff's taxes charged, credited, and paid as of June 30, 2006 in conformity with the modified cash basis of accounting.

In accordance with Government Auditing Standards, we have also issued our report dated October 2, 2007 on our consideration of the former Sheriff's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.



To the People of Kentucky
Honorable Ernie Fletcher, Governor
John R. Farris, Secretary
Finance and Administration Cabinet
Honorable Carl E. Sizemore, Clay County Judge/Executive
Honorable Edward Jordan, Former Clay County Sheriff
Honorable Kevin Johnson, Clay County Sheriff
Members of the Clay County Fiscal Court

Based on the results of our audit, we present the accompanying comments and recommendations, included herein, which discusses the following report comments:

- The Former Sheriff's Office Lacked Adequate Segregation Of Duties
- The Former Sheriff Should Have Accounted For Delinquent Franchise Taxes Correctly

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Crit Luallen", with a long horizontal flourish extending to the right.

Crit Luallen
Auditor of Public Accounts

October 2, 2007

CLAY COUNTY
EDWARD JORDAN, FORMER SHERIFF
SHERIFF'S SETTLEMENT - 2005 TAXES

June 30, 2006

	County Taxes	Special Taxing Districts	School Taxes	State Taxes
<u>Charges</u>				
Real Estate	\$ 222,877	\$ 347,687	\$ 1,346,174	\$ 389,291
Tangible Personal Property	24,901	42,963	150,854	91,014
Intangible Personal Property				42,018
Fire Protection	3,722			
Franchise Taxes	42,532	71,477	257,451	
Unmined Coal - 2005 Taxes	1,141	2,434	6,892	1,993
Additional Billings - Unmined Coal	208	324	1,255	363
Additional Billings	50	79	307	89
Oil and Gas Property Taxes	24,688	38,513	149,114	43,121
Penalties	3,335	5,192	19,920	6,399
Adjusted to Sheriff's Receipt	(110)	14	10	11
Gross Chargeable to Sheriff	323,344	508,683	1,931,977	574,299
<u>Credits</u>				
Exonerations	2,484	3,858	14,929	5,326
Discounts	3,328	5,182	19,817	7,189
Delinquents:				
Real Estate	18,706	28,851	111,706	32,303
Tangible Personal Property	2,242	3,866	13,574	1,809
Intangible Personal Property				126
Delinquent Unmined Coal	61	96	370	107
Exonerations - Unmined Coal	113	384	684	198
Uncollected Franchise Taxes	5,559	9,413	33,659	
Total Credits	32,493	51,650	194,739	47,058
Taxes Collected	290,851	457,033	1,737,238	527,241
Less: Commissions *	12,649	19,424	69,490	22,695
Taxes Due	278,202	437,609	1,667,748	504,546
Taxes Paid	278,048	437,375	1,666,834	504,280
Refunds (Current and Prior Year)	152	232	912	264
Due Districts		**		
as of Completion of Audit	\$ 2	\$ 2	\$ 2	\$ 2

* and ** See Next Page.

The accompanying notes are an integral part of this financial statement.

CLAY COUNTY
EDWARD JORDAN, FORMER SHERIFF
SHERIFF'S SETTLEMENT - 2005 TAXES
June 30, 2006
(Continued)

* Commissions:

10% on	\$	10,000
4.25% on	\$	1,265,125
4% on	\$	1,737,238

** Special Taxing District:

Due Extension District	\$	<u>2</u>
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CLAY COUNTY
NOTES TO FINANCIAL STATEMENT

June 30, 2006

Note 1. Summary of Significant Accounting Policies

A. Fund Accounting

The Sheriff's office tax collection duties are limited to acting as an agent for assessed property owners and taxing districts. A fund is used to account for the collection and distribution of taxes. A fund is a separate accounting entity with a self-balancing set of accounts. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

B. Basis of Accounting

The financial statement has been prepared on a modified cash basis of accounting. Basis of accounting refers to when charges, credits, and taxes paid are reported in the settlement statement. It relates to the timing of measurements regardless of the measurement focus.

Charges are sources of revenue which are recognized in the tax period in which they become available and measurable. Credits are reductions of revenue which are recognized when there is proper authorization. Taxes paid are uses of revenue which are recognized when distributions are made to the taxing districts and others.

C. Cash and Investments

At the direction of the fiscal court, KRS 66.480 authorizes the Sheriff's office to invest in the following, including but not limited to, obligations of the United States and of its agencies and instrumentalities, obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States, obligations of any corporation of the United States government, bonds or certificates of indebtedness of this state, and certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation (FDIC) or which are collateralized, to the extent uninsured, by any obligation permitted by KRS 41.240(4).

Note 2. Deposits

The former Sheriff maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC) as required by KRS 66.480(1)(d). According to KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge or provision of collateral should be evidenced by an agreement between the Sheriff and the depository institution, signed by both parties, that is (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution.

CLAY COUNTY
NOTES TO FINANCIAL STATEMENT
June 30, 2006
(Continued)

Note 2. Deposits (Continued)

Custodial Credit Risk - Deposits

Custodial credit risk is the risk that in the event of a depository institution failure, the Sheriff's deposits may not be returned. The former Sheriff did not have a deposit policy for custodial credit risk but rather followed the requirements of KRS 41.240(4). As of June 30, 2006 all deposits were covered by FDIC insurance or a properly executed collateral security agreement. However, as of November 14, 2005, public funds were exposed to custodial credit risk because the bank did not adequately collateralize the former Sheriff's deposits in accordance with the security agreement as follows:

- Uncollateralized and Uninsured \$151,360

Note 3. Tax Collection Period

A. Property Taxes

The real and personal property tax assessments were levied as of January 1, 2005. Property taxes were billed to finance governmental services for the year ended June 30, 2006. Liens are effective when the tax bills become delinquent. The collection period for these assessments was September 29, 2005 through June 30, 2006.

B. Oil and Gas Taxes

The oil and gas property tax assessments were levied as of January 1, 2005. Property taxes are billed to finance governmental services. Liens are effective when the tax bills become delinquent. The collection period for these assessments was November 7, 2005 (gas) and November 8, 2005 (oil) through June 30, 2006.

C. Unmined Coal Taxes

The tangible property tax assessments were levied as of January 1, 2005. Property taxes are billed to finance governmental services. Liens are effective when the tax bills become delinquent. The collection period for these assessments was April 26, 2006 through October 13, 2006.

Note 4. Interest Income

The former Clay County Sheriff earned \$1,605 as interest income on 2005 taxes. The former Sheriff distributed the appropriate amount to the school district as required by statute, and the remainder will be used to operate the Sheriff's office.

Note 5. Sheriff's 10% Add-On Fee

The former Clay County Sheriff collected \$29,542 of 10% add-on fees allowed by KRS 134.430(3). As of October 2, 2007, the former Sheriff owed \$2,375 in 10% add-on fees to his fee account. The former Sheriff collected \$81 of 10% add-on fees for 2005 unmined coal taxes. These add-on fees were used to operate the former Sheriff's office.

CLAY COUNTY
NOTES TO FINANCIAL STATEMENT
June 30, 2006
(Continued)

Note 6. Advertising Costs And Fees

The former Sheriff collected \$6,465 of advertising costs and advertising fees allowed by KRS 424.330(1) and KRS 134.440(2). The former Sheriff distributed the advertising costs to the county as required by statute, and the advertising fees were used to operate the Sheriff's office. The former Sheriff collected \$3 of advertising costs and \$15 of advertising fees for 2005 unmined coal taxes. The advertising fees were used to operate the former Sheriff's office. As of October 2, 2007, the former Sheriff owed \$1,155 in advertising costs to the county and \$840 in advertising fees to his fee account for 2005 taxes. Advertising costs of \$3 are also due to the county for 2005 unmined coal taxes.

Note 7. Unrefundable Duplicate Payments And Unexplained Receipts Should Be Escrowed

The former Sheriff should deposit any unrefundable duplicate payments and unexplained receipts in an interest-bearing account. According to KRS 393.110, the Sheriff should properly report annually to the Treasury Department any unclaimed moneys. After three years, if the funds have not been claimed, the funds should be submitted to the Kentucky State Treasurer. For the prior year taxes, the former Sheriff had \$929 in unrefundable duplicate payments and unexplained receipts. For the 2005 taxes, the former Sheriff had \$585 in unrefundable duplicate payments and unexplained receipts. Upon leaving office the former Sheriff should transfer these escrow accounts to the incoming Sheriff.

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COMMENTS AND RECOMMENDATIONS

CLAY COUNTY
EDWARD JORDAN, FORMER SHERIFF
COMMENTS AND RECOMMENDATIONS
June 30, 2006

STATE LAWS AND REGULATIONS:

The Former Sheriff Should Have Accounted For Delinquent Franchise Taxes Correctly

The former Sheriff had fourteen (14) delinquent franchise tax bills from 1998, 1999, and 2000 that have not been collected. According to KRS 136.050(1), corporations are required to pay taxes "at the same time as natural persons are required to pay taxes, and when delinquent shall pay the same rate of interest and penalties as natural persons who are delinquent." The former Sheriff should have treated delinquent franchise tax bills in a manner similar to delinquent tax bills from natural persons by turning them over to the County Clerk

Former Sheriff's Response: We were not aware delinquent franchise taxes were to be turned over to the County Clerk's office.

INTERNAL CONTROL - REPORTABLE CONDITION AND MATERIAL WEAKNESS:

The Former Sheriff's Office Lacked Adequate Segregation Of Duties

The former Sheriff's office lacked adequate segregation of duties. During our tests of receipts and disbursements, we found the following:

- Checks only had one signature.
- The former Sheriff did not recount or deposit cash.
- The former Sheriff did not compare daily bank deposits to the daily checkout sheet and receipts ledger.
- The former Sheriff did not periodically compare the bank reconciliation to the balance in the checkbook or the bank account.

The former Sheriff should have implemented the following compensating controls to offset this internal control weakness:

- Both official and a deputy should have signed all checks
- The former Sheriff should have recounted and deposited cash.
- The former Sheriff should have periodically compared a daily bank deposit to the daily checkout sheet and then compare the daily checkout sheet to the receipts ledger. Any differences should have been reconciled. The former Sheriff could have documented this by initializing the bank deposit, daily deposit, and receipts ledger.
- The former Sheriff should have periodically compared the accountant's bank reconciliation to the balance in the checkbook or bank. Any differences should have been reconciled. The former Sheriff could have documented this by initializing the bank reconciliation.

Former Sheriff's Response: I did recount cash plus checks. I did periodically compare the bank reconciliation to the balance in the checkbook. I recounted and deposited cash. I did compare bank deposits to daily checkout checks, however I did not document this on the records. I did compare the accountant's bank reconciliation to the balance in the checkbook on occasion, however I did not document this.

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REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF THE FINANCIAL
STATEMENT PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS



CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

The Honorable Carl E. Sizemore, Clay County Judge/Executive
Honorab! Edward Jordan, Former Clay County Sheriff
Honorab! Kevin Johnson, Clay County Sheriff
Members of the Clay County Fiscal Court

**Report On Internal Control Over Financial Reporting And On
Compliance And Other Matters Based On An Audit Of The Financial
Statement Performed In Accordance With Government Auditing Standards**

We have audited the former Clay County Sheriff's Settlements - 2005 Taxes as of June 30, 2006, and have issued our report thereon dated October 2, 2007. The former Sheriff prepares his financial statements in accordance with a basis of accounting other than generally accepted accounting principles. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the former Clay County Sheriff's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statement and not to provide an opinion on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statement. A reportable condition is described in the accompanying comment and recommendation.

- The Former Sheriff's Office Lacked Adequate Segregation Of Duties

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statement being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we consider the reportable condition described above to be a material weakness.



Report On Internal Control Over Financial Reporting And On
Compliance And Other Matters Based On An Audit Of The Financial
Statement Performed In Accordance With Government Auditing Standards
(Continued)

Compliance And Other Matters

As part of obtaining reasonable assurance about whether the former Clay County Sheriff's Settlement - 2005 Taxes as of June 30, 2006 is free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under Government Auditing Standards and which are described in the accompanying comments and recommendations:

- The Former Sheriff Should Have Accounted For Delinquent Franchise Taxes Correctly

This report is intended solely for the information and use of management, the Clay County Fiscal Court and the Kentucky Governor's Office for Local Development and is not intended to be and should not be used by anyone other than these specified parties.

Respectfully submitted,

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Crit Luallen
Auditor of Public Accounts

October 2, 2007

